NO. 83-2124

In the Supreme Court of the United States

OCTOBER TERM, 1983

JAMES H. RUTTER and MARIE R. RUTTER
and
J. H. RUTTER REX
MANUFACTURING COMPANY, INC.,

Petitioners,

V.

COMMISSIONER OF
INTERNAL REVENUE SERVICE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

Petitioners apply for a writ of certiorari to the United States Court of Appeals for the Fifth Circuit for review of the following questions:

I. Resolving the inter-Circuit conflicts as to whether the word "decision" in Internal Revenue Code Section 7482(a) encompasses only orders of the Tax Court that dismiss the proceedings before it or formally determine a deficiency or the lack of a deficiency within the meaning of Internal Revenue Code 7459(c), or whether it includes final orders of the Tax Court;

II. Whether the Court of Appeals erred as a matter of law in concluding that the Tax Court's Order of December 12, 1983 (Judge Simpson) regarding the shifting of the burden of proof under Internal Revenue Code Section 534(a) was not an appealable "decision" under Internal Revenue Code Section 7482(a); and

III. Whether, after considering the Congressional purpose and intent for enacting Internal Revenue Code Section 534, a taxpayer should be able to have the burden finally decided before having to prepare his case for trial, without the handicap of having to vastly overprepare his case if upon later appeal of the entire case the Court of Appeals reverses the Tax Court on its burden of proof Order.

STATEMENT OF INTERESTED PARTIES

Edward B. Benjamin, Jr. and Robert W. Nuzum, counsel of record for Petitioners, James H. Rutter and Marie R. Rutter and J. H. Rutter Rex Manufacturing Company, Inc., certify that the following listed persons have or may have an interest in the outcome of this case:

1. James H. Rutter
2. Marie R. Rutter
3. Eugene J. Rutter
4. J. H. Rutter Rex Manufacturing Company, Inc.
5. Commissioner of Internal Revenue Service.

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DECISIONS BELOW

TAX COURT—

1. Rutter v. Commissioner, 81 T. C. 937 (December 12, 1983).

COURT OF APPEALS—

2. Rutter v. Commissioner, __ F.2d __, (5th Cir. 1984), rehearing en banc denied (April 6, 1984).

JURISDICTION

This appeal raises questions of law under the Internal Revenue Code of 1954 (hereinafter "Internal Revenue Code"), as amended, 26 U.S.C. §7482(a).

The decision of the United States Court of Appeals for the Fifth Circuit (hereinafter "Fifth Circuit") at issue was entered on March 8, 1984. The Application for Rehearing En Banc was denied by the Fifth Circuit in an Order entered on April 6, 1984.

This Court has jurisdiction pursuant to 28 U.S.C. §1254(1).

STATUTES INVOLVED

This Petition raises issues under the following provisions of the Internal Revenue Code, as amended ["IRC"]:

IRC, 26 U.S.C. §7482(a)

Section 7482. COURTS OF REVIEW.

(a) JURISDICTION—The United States Court of Appeals (other than the United States Court of Appeals for the Federal Circuit) shall have exclusive jurisdiction to review the *decisions* of the Tax Court, except as provided in section 1254 of Title 28 of the United States Code, in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury; and the judgment of any such court shall be final, except that it shall be subject to review by the Supreme Court of the United States upon certiorari, in the manner provided in section 1254 of Title 28 of the United States Code. (Emphasis supplied).

* * *

IRC, 26 U.S.C. §7459(c)

Section 7459. REPORTS AND DECISIONS.

* * *

(c) DATE OF DECISION.—A decision of the Tax Court (except a decision dismissing a proceeding for lack of jurisdiction) shall be held to be rendered upon the date that an order specifying the amount of the deficiency is entered in the records of the Tax Court or, in the case of a declaratory judgment proceeding under part IV of this subchapter, or under Section 7428 or in the case of an action brought under section 6226 or section 6228(a), the date of the court's order entering the decision. If the Tax Court dismisses a proceeding for reasons other than lack of jurisdiction and is unable from the record to determine the amount of the deficiency determined by the Secretary, or if the Tax Court dismisses a proceeding for lack of jurisdiction, an order to that effect shall be entered in the records of the Tax Court, and the decision of the Tax Court shall be held to be rendered upon the date of such entry.

IRC, 26 U.S.C. §534(a)-(c)

Section 534. BURDEN OF PROOF.

(a) GENERAL RULE.—In any proceeding before the Tax Court involving a notice of deficiency based in whole or in part on the allegation that all or any part of the earnings and profits have been permitted to accumulate beyond the reasonable needs of the business, the burden of proof with respect to such allegation shall—

(1) if notification has not been sent in accordance with subsection (b), be on the Secretary, or

(2) if the taxpayer has submitted the statement described in subsection (c), be on the Secretary with respect to the grounds set forth in such statement in accordance with the provisions of such subsection.

(b) NOTIFICATION BY SECRETARY.—Before mailing the notice of deficiency referred to in subsection (a), the Secretary may send by certified mail or registered mail a notification informing the taxpayer that the proposed notice of deficiency includes an amount with respect to the accumulated earnings tax imposed by section 531.

(c) STATEMENT BY TAXPAYER.—Within such time (but not less than 30 days) after the mailing of the notification described in subsection (b) as the Secretary may prescribe by regulations, the taxpayer may submit a statement of the grounds (together with facts sufficient to show the basis thereof) on which the taxpayer relies to establish that all or any part of the earnings and profits have not been permitted to accumulate beyond the reasonable needs of the business.

* * *

Tax Court Rule 142. BURDEN OF PROOF.

* * *

(e) Accumulated Earnings Tax: Where the notice of deficiency is based in whole or in part on an allegation of accumulation of corporate earnings and profits beyond the reasonable needs of the business, the burden of proof with respect to such allegation is determined in accordance with Code

> Section 534. If the petitioner has submitted to the respondent a statement which is claimed to satisfy the requirements of Code Section 534(c), the Court *will* ordinarily on timely motion filed after the case has been calendared for trial, *rule prior to the trial* on whether such statement is sufficient to shift the burden of proof to the respondent to the limited extent set forth in Code Section 534(a)(2). (Emphasis supplied).

STATEMENT OF THE CASE

James H. and Marie R. Rutter (hereinafter "Rutter") own 100% of the outstanding stock of the J. H. Rutter Rex Manufacturing company, Inc. (hereinafter "Rutter Rex"), a Louisiana corporation engaged in the clothing manufacturing business.

On May 21, 1981, the Commissioner of Internal Revenue (hereinafter "the Commissioner" or "Respondent") issued to Rutter Rex, pursuant to Internal Revenue Code Section (hereinafter "Section") 534(b), notification that the assessment of a deficiency based upon the imposition of the accumulated earnings tax was contemplated with respect to the years 1976, 1977, 1978 and 1979. On August 21, 1981, Rutter Rex timely submitted a statement pursuant to Section 534(c) on which it relied to establish that no part of its earnings and profits was accumulated beyond the reasonable needs of the business with respect to the years 1976 through 1979. On December 17, 1981, Respondent mailed a statutory notice of deficiency to Rutter Rex, and the notice of deficiency determined, in part, an accumulated earnings tax under Section 531 of $446,658.00 for 1977 and $598,077.00 for 1978. On March 17, 1982, Rutter Rex filed a petition with the United States Tax Court (hereinafter "Tax Court") contesting the

deficiency determinations contained in the statutory notice of deficiency.

On August 16, 1983, Rutter Rex filed with the Tax court a motion for ruling on the burden of proof with respect to the retention of earnings. On October 5, 1983, a hearing was held before Judge Simpson of the Tax Court with respect to this motion. On December 12, 1983, Judge Simpson rendered a *decision*—that is a *final*, rather than an interlocutory, order—denying Rutter Rex's motion to shift the burden of proof with respect to the first five grounds asserted in its Section 534(c) statement and granting the motion with respect to the remaining two grounds asserted in its statement.

On December 23, 1981, Rutter and Rutter Rex (hereinafter "Petitioners") filed a notice of appeal, appealing the decision of the Tax Court to the Fifth Circuit. On February 3, 1984, Petitioners filed their Original Brief with the Fifth Circuit. On February 18, 1984, Petitioners were served with a copy of Respondent's Motion to Dismiss the Appeal for Lack of Jurisdiction, and on February 21, 1984 Petitioners filed their Memorandum in Opposition to Respondent's Motion to Dismiss the Appeal.

On appeal, the Fifth Circuit granted Respondent's Motion to Dismiss for Lack of Jurisdiction. The Fifth Circuit denied Petitioners' request for rehearing en banc on April 6, 1984.

Petitioners now petition for a writ of certiorari from the decision of the Fifth Circuit.

ARGUMENT

I. THERE IS A CONFLICT AMONG THE CIRCUIT COURTS OF APPEAL AS TO THE PROPER INTERPRETATION OF THE WORD "DECISION" IN SECTION 7482(a).

The United States Courts of Appeal for the Third, Sixth and Ninth Circuits interpret the word "decision" as including *all* final orders of the Tax Court, while the United States Courts of Appeal for the First, Second, Fourth and Fifth Circuits interpret the word "decision" as encompassing only those actions specified in Section 7459(c).

The Third, Sixth and Ninth Circuit Courts of Appeal have concluded that any final Tax Court order constitutes a "decision" under Section 7482(a). These circuits have expressly rejected a narrow interpretation of the word "decision" under Section 7482(a) and have held that an appellate court has jurisdiction to review *any* final order of the Tax Court.

The cases decided by the Third, Sixth and Ninth Circuits involved Tax Court orders: (1) denying a motion for summary judgment (*Ryan v. Commissioner,* 680 F.2d 324 (3d Cir. 1982)); (2) denying a motion to intervene (*Sampson v. Commissioner,* 710 F.2d 262 (6th Cir. 1983), *Estate of Dixon v. Commissioner,* 666 F.2d 386 (9th Cir. 1982), *Estate of Smith v. Commissioner,* 638 F.2d 665 (3d Cir. 1981)); (3) denying a motion to amend a petition (*Wilson v. Commissioner,* 564 F.2d 1317 (9th Cir. 1977)); (4) granting a motion to strike amended replies and affirmative defenses in an answer (*Licavoli v. Commissioner,* 318 F.2d 281 (6th Cir. 1963), *Commissioner v. S. Freider & Sons Company,* 228 F.2d 478 (3d Cir. 1955)); and (5) granting a motion to

take a deposition (*Louisville Builders Supply Company v. Commissioner*, 294 F.2d 333 (6th Cir. 1961)). *See also Commissioner v. Blue Diamond Coal Company*, 230 F.2d 312 (6th Cir. 1956). The holding in each of these cases is that *all final* orders of the Tax Court, as distinguished from interlocutory orders, *are* appealable "decisions" under Section 7482(a).

On the other hand, the First, Second, Fourth and Fifth Circuits have interpreted "decision" in Section 7482(a) to include only actions of the Tax Court that: (1) dismiss the proceedings before the court because of lack of jurisdiction, or (2) finally determine the amount of a tax deficiency or the lack of a deficiency. *See, e.g., Porter v. Commissioner*, 453 F.2d 1231 (5th Cir. 1972) (order dismissing action as to wife for deficiences when husband filed separate returns not a "decision"); *Handshoe v. Commissioner*, 252 F.2d 328 (4th Cir. 1958) (order denying taxpayers' motion to withdraw petition not a "decision"); *Commissioner v. Smith Paper, Inc.*, 222 F.2d 126 (1st Cir. 1955) (order granting taxpayer's motion to dismiss Commissioner's claim for additional excess profits taxes not a "decision"); *Kiker v. Commissioner*, 218 F.2d 389 (4th Cir. 1955) (order denying taxpayer's motion to declare deficiency notice invalid not a "decision"); and *Michael v. Commissioner*, 56 F.2d 825 (2d Cir. 1932), *cert. denied*, 296 U.S. 579 (1935) (order denying taxpayers' motion for decision of no deficiency not a "decision").

In the instant case, the Fifth Circuit adopted the position of the First, Second and Fourth Circuits. Although the Fifth Circuit did not issue written reasons to support its dismissal of Petitioners' appeal, its dismissal was based on the grounds that the word "decision" under Section 7482(a) includes only those actions specified in Section

7459(c). See Respondent's Motion to Dismiss Appeal, Appendix C to Petition for Writ of Certiorari.

Prior to its decision in this case the Fifth Circuit itself had adopted inconsistent positions with respect to the interpretation of the word "decision" in Section 7482(a). In *Commissioner v. Seminole Manufacturing Company*, 233 F.2d 395 (5th Cir. 1956), the Fifth Circuit held that an order of the Tax Court dismissing a pleading of the Commissioner *constituted* an appealable "decision" under Section 1141(a) of the Internal Revenue Code of 1939 (predecessor of Section 7482(a), containing the same language). In *Seminole Manufacturing* the Fifth Circuit specifically stated that its holding would conflict with the First Circuit's holding in *Commissioner v. Smith Paper, Inc., supra*, and therefore *refused* to follow the First Circuit's *Smith Paper* interpretation of the word "decision" that restricted it to the actions referred to in Section 7459(c). However, in *Porter v. Commissioner, supra*, the Fifth Circuit ignored its prior holding in *Seminole Manufacturing* and inconsistently held that a Tax Court order was not a "decision" under Section 7482(a) since it did not satisfy the Section 7459(c) test of either dismissing the proceedings for lack of jurisdiction or of determining the presence or absence of a deficiency.

The United States Supreme Court has never interpreted the word "decision" under Section 7482(a), but it has interpreted Section 1141 of the 1939 Code (the predecessor of, and containing the same language as, Section 7482(a)) in an *expansive* manner by permitting review of matters which were not directly revenue issues. In *United States v. California Eastern Line, Inc.*, 348 U.S. 351, 355 (1955), this Honorable Court held that Section 1141 of the 1939 Code, which vests Courts of Appeals with

"exclusive jurisdiction to review the decisions of the Tax Court," authorized review of Tax Court renegotiation orders which *neither* specified the presence or absence of a deficiency, nor dismissed the proceedings for lack of jurisdiction. Nonetheless, this Honorable Court determined that the Tax Court decision *was* reviewable under Section 1141 of the 1939 Code. At the time of its decision in *California Eastern*, this Honorable Court was aware of the Second Circuit's decision in *Michael v. Commissioner*, 56 F.2d 825 (2d Cir. 1932), *cert. denied*, 296 U.S. 579 (1935), which held that the word "decision" in Section 1003(a) of the Revenue Act of 1926 (the predecessor of Sections 1141(a) of the 1939 Code and 7482(a), and containing the same language) *was* limited to the two types of "decisions" contained in Section 601(d) of the Revenue Act of 1928 (one of the predecessors of Sections 1117(c) of the 1939 Code and 7459(c)).

In the instant case, the Fifth Circuit accepted the position of Respondent that the word "decision" under Section 7482(a) includes only those actions specified in Section 7459(c), and consequently dismissed Petitioners' appeal for lack of jurisdiction. The Fifth Circuit's decision in the instant case, which summarily dismissed Petitioners' appeal for lack of jurisdiction, therefore is contrary to the interpretation of the word "decision" as adopted by the United States Courts of Appeal for the Third, Sixth and Ninth Circuits and conflicts with the expansive interpretation by this Honorable Court of Section 1141 of the 1939 Code (the predecessor of Section 7482) in *United States v. California Eastern Line, Inc., supra.*

Petitioners respectfully submit that this Honorable Court should grant certiorari in the instant case and resolve the conflict among the Circuit Courts of Appeal as

to the proper definition of the word "decision" in Section 7482(a). This conflict as to the proper interpretation of the word "decision" arose no later than 1956 in *Commissioner v. Blue Diamond Coal Co., supra,* and continues up to the present date as evidenced by the jurisprudence cited above and now by the Fifth Circuit's decision in the instant case.

II. THE FIFTH CIRCUIT APPLIED AN INCORRECT INTERPRETATION OF THE WORD "DECISION" IN SECTION 7482(a) IN DISMISSING PETITIONERS' APPEAL.

The Fifth Circuit accepted the position of Respondent that the word "decision" in Section 7482(a) includes only those actions specified in Section 7459(c), and dismissed Petitioners' appeal for lack of jurisdiction. Petitioners submit that the Fifth Circuit applied an incorrect interpretation of the word "decision" by limiting it to actions listed in Section 7459(c), and that the correct interpretation is to define "decision" under Section 7482(a) as encompassing *all final* orders of the Tax Court.

Section 7459(c) does not attempt to define the word "decision"; instead, it addresses the *date* on which *certain types of decisions* are rendered by the Tax Court for purposes of appeal. If Congress had intended to limit the definition of "decision" for purposes of Section 7482(a) only to those actions enumerated in Section 7459(c), Congress would have done so in precise language and by cross-referencing Section 7482(a) with Section 7459(c). Congress did not intend that such an interpretation be inferred from the language of a subsection of a statute which was only intended to fix the date to be applied to certain types of decisions. *Louisville Builders Supply Company v. Commissioner, supra* at 336, cited with approval in *Sampson v. Commissioner, supra* at

262; *Estate of Dixon v. Commissioner, supra* at 386; and *Estate of Smith v. Commissioner, supra* at 665.

In 1961 the Sixth Circuit stated in *Louisville Builders Supply Co. v. Commissioner, supra* at 336, that:

> "The Commissioner here asserts that the order granting leave to take von Siebenthal's deposition is not a decision of the Tax Court. He argues that specific definition of 'decisions of the Tax Court' is set forth in Section 7459(c), I.R.C. 1954 (26 U.S.C.A. §7459(c)), and that such definition does not comprehend the order sought to be reviewed on this appeal. The general title of that Section is '*Reports and decisions;*' its subsection (c) entitled '*Date of decision*' contains the language which the Commissioner asserts sets strict and confining limits to the general language 'decisions of the Tax Court' contained in Section 7482(a).
>
> His argument is that unless a decision of the Tax Court can be found to fit into the language of the above quoted section, it is not a 'decision of the Tax Court;' that only where the Tax Court specifies an amount of deficiency or dismisses a petition for lack of jurisdiction or for other reasons, can its order be reviewed. Respondent's brief to this court says that by such subsection, 'Congress *** saw fit to define in precise terms just what constitutes a reviewable Tax Court decision.' We disagree. If Congress intended to make such a limiting definition of the words, 'decisions of the Tax Court' it could have done so in precise language. We are not persuaded that Congress left such an intent to be inferred from the language of a subsection of the statute which had for its only purpose the fixing of the date to be applied in certain types of decisions."

The legislative history underlying the enactment of Sections 7482(a) and 7459(c) also supports the position that the word "decision" in Section 7482(a) is not intended to be defined solely by the certain types of decisions enumerated in Section 7459(c). Section 7459(c) originated as Section 906(d) of The Revenue Act of *1924*. 43 Statutes At Large 253, 336 (1924). Section 906(d) contained language identical to the language now found in Section 7459(c), and predates the predecessor of Section 7482(a). The legislative history to Section 906(d) of The Revenue Act of 1924 does not indicate that Congress intended to define the word "decision" in Section 906(d) of The Revenue Act of 1924 by its listing enumerated therein. *See, e.g.*, H. Rep. No. 179, 68th Cong., 1st Sess. 1, 7-8 (1924); S. Rep. No. 398, 68th Cong., 1st Sess. 1, 42 (1924); and H. Conf. Rep. No. 844, 68th Cong., 1st Sess. 1, 30 (1924).

Section 7482(a) originated as Section 1003(a) of The Revenue Act of *1926*. 44 Statutes At Large 9, 110 (1926). Section 1003(a) contained language identical to the language now found in Section 7482(a), except for minor word changes not relevant herein. The legislative history to Section 1003(a) of The Revenue Act of 1926 also does not support the position that Congress intended the word "decision" in Section 1003(a) to be defined by the listing enumerated in the previously enacted Section 906(d). *See, e.g.*, H. Rep. No. 1, 69th Cong., 1st Sess. 1, 19 (1926); S. Rep. No. 52, 69th Cong., 1st Sess, 1, 36 (1926); and H. Conf. Rep. No. 356, 69th Cong., 1st Sess. 1, 53 (1926).

This Honorable Court's holding in *United States v. California Eastern Line, Inc., supra*, also supports the position that the word "decision" in Section 7482(a) should not be construed to have only the narrow meaning contained in Section 7459(c). In *California Eastern*, this Honorable

Court held that Section 1141 of the 1939 Code (the predecessor of Section 7482, and containing the same language) authorized the review of Tax Court renegotiation orders that did *not* specify the presence or absence of a deficiency or dismiss the proceedings for lack of jurisdiction, and this Honorable Court interpreted Section 7482(a) in an expansive manner by permitting review of matters that were not directly revenue issues. In discussing the provisions of Section 1141 of the 1939 Code, Justice Black stated:

> "The language of §1141 is broad enough to justify review of Tax Court renegotiation orders. And we cannot say that because the section was originally passed primarily to authorize review of decisions on matters it should be held inapplicable to decisions on other justiciable matters entrusted to the Tax Court by Congress."

348 U.S. 351, 353-354 (1955).

The Third and Sixth Circuits have interpreted this Honorable Court's holding in *United States v. California Eastern Line, Inc., supra*, as supporting their position that the word "decision" under Section 7482(a) should encompass *all final* orders of the Tax Court. *Ryan v. Commissioner, supra* at 326; *Estate of Smith v. Commissioner, supra* at 668; and *Louisville Builders Supply Co. v. Commissioner, supra* at 337. In *Estate of Smith, supra* at 668, the Third Circuit said:

> "Although *Commissioner v. Smith Paper, Inc., supra*, still retains some viability, *see, e.g., W. W. Windle Co. v. Commissioner*, 550 F.2d 43 (1st Cir.), *cert. denied*, 431 U.S. 966, 97 S.Ct. 2923, 53 L.Ed.2d 1062 (1977), many of the cases which cite

> it, in reality, address interlocutory *and not final* orders. *E.g., Licavoli v. Commissioner, supra.* No satisfactory reasoning has emerged in the *Smith* line of cases to explain why its restrictive approach to appealability is required by statute or by policy. The *Smith* philosophy runs counter to the general rule favoring reviewability of final agency action, see 5 U.S.C. §702 (1976), and the Supreme Court's expansive attitude in deciding in favor of reviewability of the Tax Court's decision in *United States v. California Eastern Line, Inc., supra.* For sound reasons a similar posture should be employed here." (Emphasis supplied).

The weight of authorities also supports the position that the word "decision" in Section 7482(a) should be interpreted as encompassing all final orders of the Tax Court, and favors a rejection of the narrow Section 7459(c) interpretation. *See, e.g., Sampson v. Commissioner, supra* at 263; *Ryan v. Commissioner, supra* at 326; *Estate of Dixon v. Commissioner, supra* at 387; *Estate of Smith v. Commissioner, supra* at 668; *Wilson v. Commissioner, supra* at 1318; *Licavoli v. Commissioner, supra* at 282; *Louisville Builders Supply Co. v. Commissioner, supra* at 336; *Commissioner v. Blue Diamond Coal Co., supra* at 312; and *Commissioner v. S. Frieder & Sons, supra* at 481.

Petitioners respectfully submit that the Fifth Circuit applied an incorrect interpretation of the word "decision" in Section 7482(a) in dismissing their appeal for lack of jurisdiction.

III. THE FIFTH CIRCUIT ERRED AS A MATTER OF LAW IN CONCLUDING THAT THE TAX COURT'S ORDER REGARDING THE SHIFTING OF THE BURDEN OF PROOF UNDER SECTION 534(a) WAS NOT AN APPEALABLE "DECISION" UNDER SECTION 7482(a).

Applying the interpretation that the word "decision" in Section 7482(a) includes all final orders of the Tax Court, a Tax Court order granting or denying a motion to shift the burden of proof to Respondent under Section 534 is a final order. Petitioners submit that such an order constitutes an appealable "decision" under Section 7482(a) when the purpose and intent of the Section 534 are analyzed. Petitioners therefore submit that the Fifth Circuit erred in concluding that the Tax Court's Order of December 12, 1983 regarding the shifting of the burden of proof under Section 534(a) was not an appealable "decision" under Section 7482(a).

Sections 531 and 532 impose an accumulated earnings tax on a corporation

> "...formed or availed of for the purpose of avoiding the income tax with respect to its shareholders or the shareholders of any other corporation, by permitting earnings and profits to accumulate instead of being divided or distributed."

In general, the burden of proof with respect to tax issues is on the taxpayer under Rule 142(a) of the Tax Court Rules. However, Section 534 contains an exception to this rule and provides that the burden of proof shifts to the Commissioner if the taxpayer submits a statement of the

grounds together with facts sufficient to show the basis on which the taxpayer relies to establish that all or any part of the earnings and profits have not been permitted to accumulate beyond the reasonable needs of the business. The purpose of Section 534 is to encourage the taxpayer to "show his hand" while the case is still under administrative consideration and to reward the taxpayer if he does by having the burden of proof shifted to the Commissioner in advance of litigation in the event that litigation becomes necessary. *Capital Sales, Inc. v. Commissioner*, 71 T. C. 416, 435 (1978), *rev'd on another issue sub nom Simon v. Commissioner*, 644 F.2d 339 (5th Cir. 1981).

Section 534 was enacted in response to complaints by taxpayers about the substantial expense and effort incurred in proving that an accumulation was for the reasonable needs of a business, and to remedy the imposition of the accumulated earnings tax by revenue agents as a threat to induce taxpayer settlement of other audit issues. In the Senate Finance Committee hearings on Section 534 the Committee reported that:

> "Your committee agrees with the House that this imposition of the burden of proof on the taxpayer has had several undesirable consequences. The poor record of the Government in the litigated cases in this area indicates that deficiencies have been asserted in many cases which were not adequately screened or analyzed. At the same time taxpayers were put to substantial expense and effort in proving that the accumulation was for the reasonable needs of the business. Moreover, the complaints of taxpayers that the tax is used as a threat by revenue agents to induce settlement on other issues appear to have a connection with the burden of proof which the taxpayer is required to

> assume. It also appears probable that many small taxpayers may have yielded to a proposed deficiency because of the expense and difficulty of litigating their case under the present rules."

S. Rep. No. 1622, 83d Cong., 2d Sess. 1, 70-71 (1954), *reprinted in* [1954] U.S. Code Cong. and Ad. News 4623, 4702 [hereinafter S. Rep. No. 1622].

In enacting Section 534, Congress did not want the taxing authorities to be second-guessing the responsible managers of corporations as to whether and to what extent profits should be distributed or retained, unless the taxing authorities were in a position to prove that their position was correct. See *Casey v. Commissioner,* 267 F.2d 26, 30 (2d Cir. 1959), where the Second Circuit stated:

> "The Commissioner of Internal Revenue then, had the burden of proof that Bankers had unreasonably accumulated profits. We think that the 1954 and 1955 enactments indicate that Congress did not want the taxing authorities to be second-guessing the responsible managers of corporations as to whether and to what extent profits should be distributed or retained, unless the taxing authorities were in a position to prove that their position was correct. This recent expression of Congress should, perhaps, have some bearing upon our approach to our review of the Tax Court's decision."

The obvious benefit derived by a taxpayer from the advance shifting of the burden of proof to the Commissioner under Section 534 is that the taxpayer need not formulate his trial evidence and strategy until the burden of proof issue is settled. The burden of proof determination under Section 534(c) has a critical bearing on the method in

which the taxpayer presents his evidence at trial that the earnings and profits were accumulated for the reasonable needs of the business. If the burden of proof issue is resolved in the taxpayer's favor, the Commissioner's burden of proof with respect to the grounds contained in the Section 534 statement is that he must establish that the earnings and profits were accumulated beyond the reasonable needs of the business. If the issue is resolved in the Commissioner's favor, the taxpayer has the burden of proof with respect to the grounds contained in the Section 534 statement, as well as all other grounds which might justify that the earnings and profits were accumulated to satisfy the reasonable needs of the business. As a result, Petitioners submit that the advance final determination of whether the burden of proof should be shifted to the Respondent under Section 534 is of critical importance.

The effect of the Fifth Circuit's dismissal of Petitioners' appeal for lack of jurisdiction is to adopt the position that a *final* "decision" in a Tax Court case *can never* be reached with respect to whether the burden of proof shifts until the substantive issue under Section 532(a) is decided at trial. Petitioners submit that such a result flies in the face of the specific Congressional purpose for enacting Section 534(c), since under this approach the taxpayer would *always* have to prepare his case for trial by presuming that the burden of proof was on him or else risk an adverse decision at trial or upon appeal for failure to present adequate evidence at trial. The taxpayer would *always* have to presume that he had the burden of proof because if he relied upon a "non-final" Tax Court ruling that the burden of proof shifted to the Commissioner and presented his case and evidence at trial accordingly, the Court of Appeals could determine that the burden of proof had not shifted to the Commissioner, that the taxpayer therefore

had not presented sufficient evidence at trial to satisfy his burden of proof, and could then hold against the taxpayer on the substantive issue.

Petitioners further submit that the specific Congressional purpose for enacting Section 534(c) also is flouted where the taxpayer relies upon a "non-final" Tax Court ruling that the burden of proof has not shifted to the Commissioner and presents his case and evidence at trial accordingly, and the Court of Appeals concludes that the burden of proof should have shifted to the Commissioner in the Tax Court proceedings. In such a situation, the taxpayer incurred substantial expenditures of time, effort and financial resources preparing for and presenting evidence at trial which became unnecessary based on the Court of Appeals' later ruling regarding the burden of proof. Further, the Tax Court's decision would constitute "reversible error" and result in a remand of the case to the Tax Court since the decision would have been predicated on an erroneous determination regarding the burden of proof. Petitioners submit that these results directly conflict with the stated Congressional purposes for the enactment of Section 534(c), which are to encourage the taxpayer to "*show his hand*" while the case is under administrative consideration, to reward him if he does so by having the burden of proof shift to the Commissioner, and to decrease the substantial expense and effort incurred by a taxpayer in defending an accumulated earnings tax case. *See Capital Sales, Inc. v. Commissioner, supra.*

If this Honorable Court denies Petitioners' Writ for Certiorari, the effect of the denial is to adopt the position that a taxpayer can *never* appeal an order of the Tax Court regarding the shifting of the burden of proof under Section 534(c) until the Tax Court has decided the substantive

issue. The result of such a position is to require that the taxpayer *always* prepare his case for trial by presuming that the burden of proof is on him or else risk an adverse decision for failing to present adequate evidence at trial. Petitioners submit that such a result would be absurd and would frustrate and fly in the face of the Congressional intent and purposes for which Section 534(c) was enacted. *See* S. Rep. No. 1622, *supra.*

IV. TAX COURT RULE 142(e) NOW SPECIFICALLY PROVIDES FOR AN ADVANCE DETERMINATION OF THE BURDEN OF PROOF, AND THEREFORE THE INSTANT CASE IS DIFFERENT FROM THE PREVIOUS CASES WHICH RESTRICTIVELY CONSTRUED "DECISION" IN SECTION 7482(a).

The pertinent language in Section 534(a) and (c), which provides for shifting the burden of proof to the Commissioner, was enacted in 1954 for the reasons stated above. S. Rept. No. 1622, *supra.* However, there was no Tax Court Rule permitting an *advance and final* ruling on this issue until 1974. Prior to 1974, the Tax Court did not rule in advance of trial as to whether a taxpayer's Section 534(c) statement was sufficient to shift the burden of proof to the Commissioner, but would only rule with respect to this issue at trial. *See, e.g., Shaw-Walker Company v. Commissioner,* 39 T. C. 293 (1962).

Tax Court Rule 142(e), which became effective on January 1, 1974, provides that the Tax Court will ordinarily *rule prior to trial* on whether a taxpayer's Section 534(c) statement is sufficient to shift the burden of proof to the Commissioner. Tax Court Rules of Practice and Procedure, reprinted in 60 T.C. 1057, 1134 (1973). Petitioners are

aware of only one other reported decision where the Tax Court decided the burden of proof issue in a separate proceeding prior to the trial, and in that case the Tax Court held that the burden of proof shifted to the Commissioner and the Commissioner did not appeal the order. *Soros Associates International, Inc. v. Commissioner,* T.C. Memo. 1982-79.

By contrast to the instant case, none of the cases cited hereinabove that restrictively construed "decision" involved a situation in which the Tax Court Rules provided for a determination in *advance* of trial. The instant case is the first case to address whether a Tax Court *advance and final* order constitutes a "decision" in Section 7482(a).

The specific purposes for Section 534(c) and Tax Court Rule 142(e) are flouted if the Fifth Circuit's dismissal of Petitioners' appeal for lack of jurisdiction is upheld. Contrary to the specific directions of Rule 142(e), the effect of the Fifth Circuit's dismissal is to adopt the position that a *final* "decision" in a Tax Court case *can never* be reached with respect to whether the burden of proof shifts until the substantive issue is decided at trial.

In summary, Petitioners respectfully request that this Honorable Court grant their Petition For Writ of Certiorari, resolve the inter-Circuit conflicts as to the definition of the word "decision" under Section 7482(a), conclude that the Tax Court's Order of December 12, 1983 constitutes a final "decision" under Section 7482(a); and remand this case to the Fifth Circuit for it to determine whether the Tax Court's decision was correct.

CONCLUSION

For these reasons, a writ of certiorari should issue to review the decision of the United States Court of Appeals for the Fifth Circuit.

Respectfully submitted,

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CERTIFICATE OF SERVICE

We hereby certify that on this 23rd day of June, 1984 three copies of this Petition for Writ of Certiorari were mailed, postage prepaid, to all counsel of record in this matter.

Edward B. Benjamin, Jr.
EDWARD B. BENJAMIN, JR.

Robert W. Nuzum
ROBERT W. NUZUM

APPENDIX "A"

81 T. C. No. 58

UNITED STATES TAX COURT

JAMES H. RUTTER and MARIE R. RUTTER,

Petitioners

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

J. H. RUTTER REX MANUFACTURING CO., INC.,

Petitioner

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

Docket Nos. 15061-81,
6343-82.

Filed December 12, 1983.

(1) P, a corporation, moved for a pretrial ruling that its statement submitted in accordance with sec. 534(c), I.R.C. 1954, relating to the grounds for the accumulation of its earnings and profits, was sufficient to shift the burden of proof to the Commissioner. *Held:* (a) The opportunity for or the occurrence of discovery in accordance with the Rules of the Tax Court does not affect the scope of the facts that must be included in such

statement to support the grounds alleged. (b) As to the first five grounds asserted, P's sec. 534(c) statement fails to set forth facts sufficient to show the basis of such grounds. As to the last two grounds asserted, P's sec. 534(c) statement does set forth facts sufficient to show the basis thereof.

(2) P moved to compel production of two documents. *Held:* (a) As to the first document, since P's officers have supplied affidavits to the Commissioner regarding their recollection of the events which are the subject of such document, possible impeachment use is no longer an adequate ground to resist production of this document. (b) As to the second document, the Commissioner's assertion of executive privilege is sustained.

Edward B. Benjamin, Jr., for the petitioners, and *Robert W. Nuzum,* for the petitioner in docket No. 6343-82.

H. Karl Zeswitz, Jr., for the respondent.

OPINION

SIMPSON, *Judge:* This matter is before the Court on the petitioner's motion under Rule 142(e) of the Tax Court Rules of Practice and Procedure[1] for a ruling, prior to trial, on the sufficiency of the petitioner's statement under section 534(c) of the Internal Revenue Code of 1954[2] and on

[1] Any reference to a Rule is to the Tax Court Rules of Practice and Procedure.

[2] All statutory references are to the Internal Revenue Code of 1954 as in effect during the years in issue.

the petitioners' motion under Rule 50(b) to compel production of two documents.

In accordance with section 534(b), the Commissioner notified J. H. Rutter Rex Manufacturing Co., Inc. (the petitioner), that he proposed to issue a notice of deficiency for the taxable years 1976, 1977, 1978, and 1979 which would include an amount with respect to the accumulated earnings tax imposed by section 531. The petitioner timely submitted a statement pursuant to section 534(c). Thereafter, the Commissioner issued a notice of deficiency determining an accumulated earnings tax under section 531 of $446,658 for 1977 and $598,077 for 1978. The notice of deficiency claimed no accumulated earnings tax for 1976 or 1979.

In his notice of deficiency, the Commissioner found that the petitioner retained current earnings and profits of $1,188,723 in 1977 and $1,582,018 in 1978 and determined that such amounts were subject to the section 531 tax. In his answer, the Commissioner alleges that the petitioner had an accumulated surplus of $4,843,050 in 1977 and $5,135,415 in 1978, that the petitioner paid no dividends in the years 1974 through 1979, and that if the petitioner had distributed its accumulated earnings and profits in 1977 and 1978, its shareholders would have paid an additional $1,103,911 in personal income taxes.

Section 534(c) provides that "the taxpayer may submit a statement on the grounds (together with facts sufficient to show the basis thereof) on which it relies to establish that all or any part of its earnings and profits have not been permitted to accumulate beyond the reasonable needs of the business," and if such a statement is submitted, section 534(a)(2) provides that the burden of proof shall be on the Commissioner with respect to the

grounds set forth in such statement. *Capital Sales, Inc. v. Commissioner,* 71 T. C. 416, 435 (1978), revd. and remd. on another issue sub nom. *Simon v. Commissioner,* 644 F.2d 339 (5th Cir. 1981). Rule 142(e) provides that the Court will ordinarily, on motion, rule prior to trial on whether a section 534(c) statement submitted by the taxpayer is sufficient to shift the burden of proof to the Commissioner pursuant to section 534(a)(2).

For a statement under section 534(c) to shift the burden of proof to the Commissioner, the statement:

> must constitute more than mere notice of an intent to prove the reasonableness of the accumulation. Rather, the taxpayer must show its hand by stating with clarity and specificity the grounds on which it will rely to prove reasonable business needs, and by setting out the facts (not the evidence, but more than conclusions of law) that, if proven, support the alleged business needs for the accumulation. [B. Bittker & J. Eustice, Federal Income Taxation of Corporations and Shareholders, par. 8.08, p. 8-33 (4th ed. 1979); footnote omitted.]

Section 534 and our cases emphasize the need for the taxpayer to present sufficient facts to support the grounds alleged. Sec. 534(c); *Capital Sales, Inc. v. Commissioner,* 71 T.C. at 435-436; *Chatham Corp. v. Commissioner,* 48 T.C. 145, 146-147 (1967); *I. A. Dress Co. v. Commissioner,* 32 T.C. 93, 100-101 (1959), affd. on other grounds 273 F.2d 543 (2d Cir. 1960).

The petitioner is a clothing manufacturer. It presents in its section 534(c) statement seven grounds to support its contention that its earnings and profits were

not permitted to accumulate beyond the reasonable needs of the business. Its first ground is that earnings and profits had to be accumulated to supply working capital necessary to conduct normal business operations. In support of such ground, the statement recites the history of the corporation from its formation in the 1930s to its present multiplant operation which supplies a number of large retail establishments. The statement alleges that contracts between the petitioner and a major customer, a company that accounted for 70 percent of the petitioner's business during the period 1976 through 1979, required the petitioner to keep large amounts of cash on hand. The arrangement between this customer and the petitioner required the petitioner to purchase and pay the customer for piece goods. The petitioner then manufactured finished goods which were placed in the petitioner's inventory awaiting shipping orders from the customer. After the finished goods were shipped, the petitioner billed and received payment from the customer. The petitioner's statement maintains that this cycle usually took about 3 months, but that "in many instances," the cycle had taken up to a year.

The petitioner's statement alleges that during the period from December 1974 to October 1975, it accumulated a large finished goods inventory, valued at $8,500,000 on December 31, 1974, and that its profits for the first half of 1975 were only $1,200. The petitioner's cash reserves during this period were insufficient to meet its piece goods obligations with its customer, and as a result, the petitioner's relationship with this customer deteriorated. Additionally, the statement alleges that this cash shortage cost the petitioner approximately $90,000 in lost cash discounts and interest charges incurred in its own purchases. The petitioner's statement concludes that these "unpredictable fluctuations of orders and accumulations of

inventory for which the Company is not compensated" warranted its accumulation of earnings and profits.

In the statement, the petitioner declares that "following the critical cash flow problem that occurred in 1974-1975," it built up its cash reserves because of additional business it expected from its then major customer and from a large new customer. At the end of 1980, the petitioner learned that its major customer might be decreasing its orders from the petitioner, and soon thereafter, the petitioner was informed that such decrease in business indeed would occur. The statement alleges that at this time the petitioner had to either find another customer the size of the one it was losing or liquidate the business. The petitioner did subsequently locate a suitable replacement customer. Its statement recites that as of August 1, 1981, 4 months after having contracted with the new customer, the petitioner only had accounts payable of approximately $1,000,000, cash and certificates of deposit of $1,500,000, and accounts receivable (not yet due) of $4,500,000. The statement further alleges that the petitioner would not have been able to secure the new business had it not been able to "finance" its new customer. The statement says that the petitioner's profit margin on the new account was 15 percent and that such profit would have been eliminated had the petitioner been forced to borrow money at 20.5 percent. The petitioner concludes the first section of its statement by reiterating that it is in a volatile industry where it must finance the orders placed by its customers and that "The only way for a business to survive in this industry is to have a substantial amount of cash reserves on hand to meet the consistent unpredictable nature of the industry."

The Commissioner argues that the grounds and

supporting facts asserted in the petitioner's section 534(c) statement are inadequate to shift the burden of proof. He contends that the grounds are "either irrelevant or insufficient to justify petitioner's accumulation of the earnings and profits." He describes the petitioner's assertions regarding the necessity to "finance" new customers as "vague, indefinite and incomplete."

In response to the Commissioner's contentions, the petitioner argues that its section 534(c) statement satisfies the sufficiency standard articulated by the Fifth Circuit in *Motor Fuel Carriers, Inc. v. Commissioner*, 559 F.2d 1348, 1352 (1977), revg. a Memorandum Opinion of this Court:

> We think § 534's language indicates that the statement simply serves a notice function. Whether the "grounds" divulged in the statement subsequently proved convincing is irrelevant to this function. We have examined *** [the taxpayer's] statement and conclude that it gave the government a sufficiently specific idea of how *** [the taxpayer] planned to proceed at trial. *** It is true, as the government observes, that the statement failed to break down the 1968-1970 cost projections into "component costs." But just as the statement is not supposed to be legally sufficient on the question of definiteness, neither is it supposed to be a substitute for testimony at trial.***

We have carefully considered the petitioner's section 534(c) statement in light of the Fifth Circuit's opinion in *Motor Fuel Carriers*. We are aware of the distinction drawn by the Court of Appeals between the factual sufficiency required of a section 534(c) statement and the factual sufficiency necessary to prevail at trial. Nevertheless, in the present case, we conclude that where the petitioner's

statement fails to provide facts sufficient to show the basis of the asserted grounds, it fails to satisfy the requirements articulated by the Fifth Circuit.[3] In *Motor Fuel Carriers*, the Fifth Circuit characterized the taxpayer's section 534(c) statement as "lengthy." We could not so characterize the petitioner's statement in the present case.[4]

As to the first ground, the petitioner's statement contains no description of net liquid assets, inventory on hand (either at the beginning or the end of the year), average inventory, net sales for the year, accounts receivable, or operating cycles. The need for working capital may constitute a sufficient ground for accumulating earnings and profits. Sec. 1.537-2(b)(4), Income Tax Regs.; *Faber Cement Block Co. v. Commissioner*, 50 T.C. 317, 329-334 (1968). However, for the petitioner to establish that it accumulated earnings and profits for such reason, it would be necessary for the petitioner to establish such facts as the amounts of its inventory during the years at issue, the operating cycle during such years, the amount of liquid assets on hand, and that during such years, it recognized a need to set aside additional earnings and profits to provide additional working capital. *Henry Van Hummell, Inc. v. Commissioner*, 364 F.2d 746, 750-751 (10th Cir. 1966), affg. a Memorandum Opinion of this Court; *Magic Mart, Inc. v. Commissioner*, 51 T.C. 775, 791-794 (1969);

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[3] Since we have concluded that the petitioner's statement is insufficient to satisfy the requirements of the *Motor Fuel Carriers* decision, we need not decide whether that case established a different standard than that followed by this Court. See *Capital Sales, Inc. v. Commissioner*, 71 T.C. 416, 435-436 (1978), revd. and remd. on another issue sub nom. *Simon v. Commissioner*, 644 F.2d 339 (5th Cir. 1981).

[4] We have examined the sec. 534(c) statement in the *Motor Fuel Carriers* case and have found that it contains substantially more supporting facts than the sec. 534(c) statement in the present case.

Faber Cement Block Co. v. Commissioner, 50 T.C. at 328-336; *John P. Scripps Newspapers v. Commissioner*, 44 T.C. 453, 467 (1965). For the statement to be sufficient, it must include at least the ultimate facts on which the petitioner will rely, and the petitioner's statement contains no such facts for 1977 and 1978.

Moreover, the petitioner has failed to explain in any more than a superficial manner the relationship of the "1974-1975 cash flow crisis" to the accumulations in the years in issue. The petitioner learned in late 1980 of the possible reduction in business received from its major customer during 1976 through 1979. The statement does not explain how that decline in business accounted for the accumulations during 1977 and 1978, other than as an illustration of the assertion that the petitioner was involved in an "unpredictable" business. Because of this lack of supporting facts concerning 1977 and 1978, the tax years in issue, the petitioner's statement fails to satisfy the requirements of section 534(c) as to the first ground.

As its second ground, the petitioner asserts that it accumulated earnings and profits in 1977 and 1978 for replacement and improvement of fixed assets. In support thereof, the petitioner's statement alleges that during the period 1976 through 1979 it was actively seeking new customers in order to reopen its New Orleans pants plant. It entered into "preliminary agreements" with a customer to manufacture pants and, as a result, planned improvements to the pants plant during 1976 through 1979. However, the only expenditures listed in the statement, actual or contemplated, were $495,612, in cash, in 1979 for plant improvements, most of which was spent on the New Orleans pants plant, and $250,000, in cash, in 1977 for an electronic cloth pattern marking machine. The Commissioner asserts that the statement

fails to set forth "facts which are substantial, material, definite and clear, showing that in 1977 and 1978 concrete plans existed for the replacement and improvement of fixed and movable assets." The Commissioner terms the purchase of the electronic marking machine "irrelevant" since it was purchased for cash prior to the end of 1977.

The regulations under section 537 provide that the reasonable needs of the business include reasonably anticipated needs of the business. However, in order to justify an accumulation of earnings and profits, "the corporation must have specific, definite, and feasible plans for the use of such accumulation." Sec. 1.537-1(b)(1), Income Tax Regs. Such section further provides:

> Such an accumulation need not be used immediately, nor must the plans for its use be consummated within a short period after the close of the taxable year, provided that such accumulation will be used within a reasonable time depending upon all the facts and circumstances relating to the future needs of the business. Where the future needs of the business are uncertain or vague, where the plans for the future use of an accumulation are not specific, definite, and feasible, or where the execution of such a plan is postponed indefinitely, an accumulation cannot be justified on the grounds of reasonably anticipated needs of the business.

To shift the burden of proof, a statement need not contain sufficient evidence to prove the ground set forth therein. *Chatham Corp. v. Commissioner,* 48 T.C. at 146-147. However, section 534(c) explicitly requires that in order to shift the burden of proof with regard to the ground, the statement must provide facts sufficient to

show the basis of the asserted ground. Here, we have no facts concerning the assets to be replaced or improved in 1977 or 1978, no facts indicating any specific plans in 1977 or 1978 for the replacement or improvement of assets, and no facts reflecting any decisions in 1977 or 1978 to set aside specific amounts of accumulated earnings and profits for the replacement or improvement of assets. Moreover, the ongoing negotiations intended to provide more business for the New Orleans pants plant had yielded no definite plans for improvements as of the submission of the petitioner's statement on August 21, 1981. Thus, we conclude that the statement is insufficient as to the second ground.

In its statement to justify its accumulation of earnings and profits, the petitioner's third ground is the development, production, and distribution of products. Therein the petitioner asserts that as a result of having retained earnings and profits, it was among the first to manufacture permanent press clothing. The statement recites: "This process had required large amounts of cash and several different attempts before it was made to work. This expenditure had reinforced the need for maintaining large capital reserves." However, the statement contains no facts showing any need for the accumulation of earnings and profits in 1977 or 1978 for this purpose. In fact, the petition states that in 1965 the petitioner began selling permanent press clothing. The petitioner's section 534(c) statement also asserts that it needed to replace its fleet of five trucks which are usually replaced every 3 years. The total cost of replacing the trucks is listed as approximately $375,000. Yet, the statement contains no facts showing any plans in 1977 or 1978 to replace the trucks or showing whether or when the trucks have in fact been replaced. Under such circumstances, we find that the petitioner's statement fails to contain sufficient facts to support its third ground.

As a fourth ground for its accumulation of earnings and profits, the petitioner's section 534(c) statement says that it feared a disruption in its business due to potential labor troubles. According to the statement, the petitioner experienced a 12-month labor strike in 1954. In 1975, a union election was held at the petitioner's Columbia, Miss., plant in which the union was defeated. From these two events and the assertion that two other New Orleans area companies that had accepted unionization and "shortly thereafter went bankrupt or were forced to sell out," the statement alleges that the accumulation of earnings and profits was necessary "in part" to counter the possibility of labor problems.

The Commissioner points out that no specific amount of the retained earnings and profits is allocated in the statement to the possibility of labor problems. In addition, the statement does not attempt to estimate the cost of hiring new workers or the amount of anticipated losses resulting from labor problems. The Commissioner also contends that there was no attempt to set forth sufficient facts to show the likelihood of labor problems in 1977 and 1978. We agree with the Commissioner. Again, the petitioner's statement fails to set forth sufficient facts in support of its fourth ground.

The fifth ground in the petitioner's statement is that earnings and profits were accumulated to have funds available in the event the petitioner secured new business from the United States Government. In support of this ground, the statement alleges that during the 1970s the petitioner was unable to bid on certain Federal clothing contracts because of small business set-asides. Federal regulations restrict eligible bidders on Federal contracts, in some cases, to companies having less than 500 employees.

The petitioner had more than 500 employees. In litigation in which the petitioner was involved during 1976 through 1979, the petitioner challenged these regulations. As of the submission of the section 534(c) statement, such litigation was unresolved.

The statement asserts: "During the years in question the Company wisely accumulated funds that were needed if the Company won its litigation and acquired substantial government contracts." The Commissioner characterized this ground as "so vague, uncertain and indefinite as not to constitute a valid ground for the accumulation of any of its earnings and profits for the taxable years 1977 and 1978." He also asserted that the statement fails to delineate specific amounts of working capital necessary in the event the petitioner prevailed in the litigation and gives no specific facts concerning the status of the litigation except that it was pending during 1976 through 1979.

Our purpose is, of course, not to decide whether the ground justifies the accumulation of earnings and profits in the year at issue. However, we do agree with the Commissioner that the petitioner has again failed to set out sufficient supporting facts with regard to this ground. There were no facts reflecting any plans in 1977 or 1978 for setting aside specific amounts of accumulated earnings and profits to provide working capital for the Government business; in fact, we have no indication that there were any definite plans or hopes for actually securing such business.

In its statement of the grounds for the accumulation of earnings and profits, the petitioner includes as its sixth ground the allegation that there have been no loans to or expenditures for the benefit of shareholders and as its

seventh ground, the allegation that, except for a de minimis investment, there have been no investments in a business unrelated to that of the petitioner. Section 1.537-2(c) of the Income Tax Regulations treats the making of such loans or investments as evidence that earnings and profits are being accumulated unreasonably; nevertheless, such allegations do support, to some extent, the petitioner's contention that it did not unreasonably accumulate its earnings and profits. The petitioner cannot be expected to do more than deny that it made expenditures that would tend to evidence that it had unreasonably accumulated its earnings and profits. Accordingly, we hold that as to loans to or expenditures for the benefit of shareholders or investment by the petitioner in unrelated businesses, the burden of proof will be on the Commissioner.

Finally, the petitioner argues that in light of the discovery that is available to the Commissioner under the Rules of this Court, a section 534(c) statement is sufficient to shift the burden of proof to the Commissioner as to the grounds asserted therein if it outlines the basic facts supporting such grounds.[5] Apparently, the petitioner is arguing that in judging the sufficiency of the supporting facts in a statement under section 534(c), we should take into consideration the fact that the Commissioner can secure additional facts by means of discovery in accordance with the Rules of this Court and that because of such discovery, the supporting facts need not be set forth fully. The procedure for the submission of the statement under section

[5] The petitioner relies on *Petrozello Co. v. Commissioner*, T.C. Memo. 1983-250, on appeal (3d Cir., Aug. 5, 1983), and *Soros Associates International, Inc. v. Commissioner*, T.C. Memo. 1982-79. However, in each case, the sufficiency of a sec. 534(c) statement must be decided by an examination of the grounds and supporting facts contained therein.

534(c) was enacted as a part of the Internal Revenue Code of 1954, and at that time, there were no procedures for discovery under the Rules of the Tax Court. The procedures for discovery did not become effective until January 1, 1974 (60 T.C. 1069 (1973)), and before the adoption of such Rules, our cases consistently required that a section 534(c) statement must contain supporting facts which are substantial, material, definite, and clear. *J. Gordon Turnbull, Inc. v. Commissioner,* 41 T.C. 358, 370 (1963), affd. 373 F.2d 87 (5th Cir. 1967); *I. A. Dress Co. v. Commissioner,* 32 T.C. at 100-101.[6] Congress has taken no action to modify the statutory requirement in section 534(c) as a result of the adoption of the discovery procedures.

It may be suggested that since the Commissioner can obtain facts through discovery, there is no longer the same need to include facts in the section 534(c) statement as there was when discovery was not available, but such suggestion overlooks the purpose and operation of the procedures established by section 534. The purpose of those procedures is to encourage the taxpayer to "show its hand" while the case is still under administrative consideration; if it does, it is rewarded by having the burden of proof shifted to the Commissioner in the event that litigation becomes necessary. Sec. 534(a)(2); *Capital Sales, Inc. v. Commissioner,* 71 T.C. at 435. The effect of such procedures is to facilitate the settlement of accumulated earnings tax cases at the administrative level. *Manson Western Corp. v. Commissioner,* 76 T.C. 1161, 1163-1165 (1981); see Rev. Proc.

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[6] See also *Powder Mill Realty Trust v. Commissioner,* T.C. Memo. 1973-149; *Bohac Agency, Inc. v. Commissioner,* T. C. Memo. 1971-228; *Federal Ornamental Iron & Bronze Co. v. Commissioner,* T. C. Memo. 1969-72.

56-11, 1956-1 C.B. 1028. If the taxpayer shows its hand at the administrative level, the Commissioner will be in a position to evaluate his case, and many cases may be settled at the administrative level. However, were we to hold that the section 534(c) statement need not include supporting facts because the Commissioner could ultimately obtain such facts through discovery after a case is commenced in this Court, the incentive for the taxpayer to show its hand during the administrative process would be removed, and fewer cases would be settled at that level. Under such circumstances, we conclude that the availability of discovery should not and does not affect the scope of the facts to be included in the statement under section 534(c).

In the second motion, the petitioners seek to compel the production of two documents. The documents were submitted to the Court for its in camera inspection. Each document is a memorandum to the file written by a revenue agent who examined the petitioners' tax returns. The Commissioner, who is the objecting party, bears the burden of establishing that his objections to the petitioners' request for production should be sustained by this Court. *Branerton Corp. v. Commissioner,* 64 T.C. 191, 193 (1975).

In the first document, the agent set down his recollections of the discussions that took place when the president of the corporate petitioner executed a form 872 extending the period of limitations. The Commissioner objects to the production of this document on the ground that it may be used by him for impeachment purposes. During oral argument on this motion, we were informed by the Commissioner's attorney that certain of the petitioner's officers have filed with the Commissioner affidavits which contain their recollections of the discussions at the time of the execution of the form. In light of the fact that the

petitioner's officers have provided such affidavits to the Commissioner, we believe that possible impeachment use is no longer an adequate ground to resist production of this document. See *Zaentz v. Commissioner,* 73 T.C. 469, 479 (1979); *Industrial Electric Sales & Service, Inc. v. Commissioner,* 65 T.C. 844, 845-847 (1976); *P. T. & L. Construction Co. v. Commissioner,* 63 T.C. 404, 412-413 (1974).

The Commissioner maintains that the second document is exempted from disclosure by executive privilege, which shields from disclosure the mental impressions, opinions, reasoning, and conclusions of Government officials. He also asserts that the document was prepared in anticipation of litigation.

Executive privilege does protect some documents from disclosure, but the privilege is qualified, not absolute. Executive privilege covers:

> statements of advice, deliberation, and recommendation.***The privilege is based on the public policy of encouraging wise and efficient government by fostering an environment wherein officials may comment on issues of governmental policy- and decision-making in a candid manner, without fear that their comments will be subjected to scrutiny by the public at large.
>
> But this privilege is qualified in that it recognizes there are instances in which justice will require disclosure of such material. A balancing of interests is required; the gravity of the individual's need for disclosure must be weighed against the harm that disclosure may do to intragovernmental candor. [*P. T. & L. Construction Co. v. Commissioner,* 63 T.C. at 409.]

After having examined the revenue agent's memorandum, we have concluded that it contains only his legal theories about certain aspects of the examination of the petitioner's returns and as such constitutes the thought processes and conclusions of the revenue agent. Accordingly, we hold that it is protected from discovery by executive privilege. *Zaentz v. Commissioner, supra* at 479; *Barger v. Commissioner,* 65 T.C. 925, 930-931 (1976). In view of that conclusion, we need not determine whether the second document was prepared in anticipation of litigation. See *Dvorak v. Commissioner,* 64 T.C. 846, 848-851 (1975); *Branerton Corp. v. Commissioner,* 64 T.C. at 194; *P. T. & L. Construction Co. v. Commissioner,* 63 T.C. at 407-408.

An appropriate order will be issued.

APPENDIX "B"

UNITED STATES TAX COURT
WASHINGTON, D.C. 20217

Docket Nos. 15061-81
6343-82

JAMES H. RUTTER and MARIE R. RUTTER, ET AL.,

Petitioners

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

ORDER

Pursuant to the determination of this Court as set forth in its Opinion filed December 12, 1983, it is

ORDERED: That the petitioners' motion to shift the burden of proof, filed August 22, 1983, is hereby granted in part and denied in part in accordance with such opinion. It is further

ORDERED: That the petitioners' motion to compel Respondent to produce certain documents, filed August 29, 1983, is granted in part and denied in part in accordance with such opinion.

/s/ Charles R. Simpson
Judge

Dated: Washington, D.C.
December 12, 1983

APPENDIX "C"

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 84-4003

JAMES H. RUTTER and MARIE R. RUTTER,

Appellants

v.

COMMISSIONER OF INTERNAL REVENUE,

Appellee

J. H. RUTTER REX MANUFACTURING
COMPANY, INC.,

Appellant

v.

COMMISSIONER OF INTERNAL REVENUE,

Appellee

MOTION TO DISMISS APPEAL FOR
LACK OF JURISDICTION

The Commissioner of Internal Revenue, appellee herein, by his counsel, respectfully moves this Court to dismiss the appeal in the above-captioned case for lack of jurisdiction on the ground, as is more fully set forth in the accompanying memorandum, that the appeal was not taken from a final decision of the United States Tax Court.

Wherefore, it is respectfully requested that the Court issue an order dismissing the appeal in the above-captioned case.

GLENN L. ARCHER, JR.

GLENN L. ARCHER, JR.
Assistant Attorney General
Tax Division
Department of Justice
Washington, D.C. 20530
Counsel for the Appellee

Dated: This 15th day of February, 1984.

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 84-4003

JAMES H. RUTTER and MARIE R. RUTTER,

Appellants

v.

COMMISSIONER OF INTERNAL REVENUE,

Appellee

J. H. RUTTER REX MANUFACTURING COMPANY, INC.,

Appellant

v.

COMMISSIONER OF INTERNAL REVENUE,

Appellee

MEMORANDUM IN SUPPORT OF MOTION TO DISMISS FOR LACK OF JURISDICTION

STATEMENT

This appeal is taken by James and Marie Rutter and J. H. Rutter Rex Manufacturing Company, Inc. (taxpayers) from that part of an order of the United States Tax Court (Judge Simpson), filed on December 12, 1983 (Doc. 27),[1] that denied taxpayers' motion to shift the burden of proof. The relevant facts may be summarized as follows:

[1] "Doc." references are to the original documents as numbered by the Clerk of the Tax Court.

In accordance with Section 534(b) of the Internal Revenue Code of 1954 (26 U.S.C.), the Commissioner notified J. H. Rutter Rex Manufacturing Company, Inc. (Rutter Rex) that he proposed to issue a notice of deficiency for the 1976 through 1979 tax years, which would include an amount with respect to the accumulated earnings tax imposed by Section 531 of the Code. Rutter Rex timely submitted a statement pursuant to Section 534(c) of the Code setting forth seven grounds justifying its accumulated earnings. Thereafter, a notice of deficiency was issued to Rutter Rex determining an accumulated earnings tax liability of $446,658 for 1977, and $598,077 for 1978. (Doc. 26.)

Rutter Rex filed a petition for redetermination with the Tax Court on March 22, 1982. (Doc. 5.) On August 22, 1983, a motion to shift the burden of proof with respect to the seven grounds contained in the Section 534(c) letter was filed by taxpayers.[2] (Doc. 14.) A hearing on taxpayers' motion was held on October 5, 1983. (Doc. 23.) The Tax Court issued an order denying taxpayers' motion to shift the burden of proof with regard to the first five grounds stated therein, and granted the motion with respect to the last two grounds. (Doc. 26.) On December 23, 1983, taxpayers filed a notice of appeal from this order. (Doc. 28.)

ARGUMENT

THE APPEAL SHOULD BE DISMISSED FOR LACK OF JURISDICTION BECAUSE THE APPEAL WAS NOT TAKEN FROM A FINAL DECISION OF THE TAX COURT

Section 7482(a) of the Internal Revenue Code of 1954

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[2] Taxpayers' cases were consolidated by an order dated December 15, 1982. (Docs. A, B.)

(26 U.S.C.) provides in pertinent part as follows:

> SEC. 7482. COURTS OF REVIEW.
>
> (a) *Jurisdiction.*—The United States Courts of Appeals shall have exclusive jurisdiction to review the decisions of the Tax Court,***in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury;***.

In *Porter v. Commissioner,* 453 F.2d 1231, 1232-1233 (5th Cir. 1972), this Court interpreted Section 7482(a) to mean that only final orders of the Tax Court are appealable; interlocutory orders are not immediately appealable, but are reviewable only when review is taken of the final decision.[3] *Porter* held that two kinds of judicial action constituted final orders. First, an order of the Tax Court dismissing the proceeding before it. Second, a decision formally determining a deficiency or the lack of a deficiency. See also *Michael v. Commissioner,* 56 F.2d 825 (2d Cir. 1932); *Ceco Steel Products Corp. v. Commissioner,* 150 F.2d 698 (8th Cir. 1945); *Commissioner v. Smith Paper, Inc.,* 222 F.2d 126 (1st Cir. 1955); *Commissioner v. S. Frieder & Sons Co.,* 228 F.2d 478, 479-480 (3d Cir. 1955); *Licavoli v. Commissioner,* 318 F.2d 281 (6th Cir. 1963); *Ryan v. Commissioner,* 517 F.2d 13 (7th Cir. 1975), cert denied, 423 U.S. 892 (1975); *W. W. Windle Co. v. Commissioner,* 550 F.2d 43, 45 (1st Cir. 1977), cert. denied, 431 U.S. 966 (1977); *Wilson v. Commissioner,* 564 F.2d 1317 (9th Cir. 1977), cert. denied *sub nom. Mercer v. Commissioner,* 439 U.S. 832 (1978); *Shapiro v. Commissioner,*632 F.2d 170 (2d Cir. 1980), cert. denied, 449 U.S. 1082 (1981).

---

[3] *Commissioner v. Seminole Manufacturing Co.,* 233 F.2d 395 (5th Cir. 1956) is not to the contrary. In that case this Court allowed an appeal from an order of the Tax Court dismissing a pleading of the Commissioner that had sought to establish a deficiency.

In the instant case the order appealed from is clearly interlocutory. An order determining who has the burden of proof with respect to specified issues simply allows the parties to further develop their trial strategies. The Tax Court has yet to reach the merits of taxpayer's petition. Thus, the Tax Court has neither dismissed taxpayers' petition (or any portion thereof) nor entered a decision redetermining the asserted deficiency. Consequently, the instant appeal is premature and must be dismissed for lack of jurisdiction.

GLENN L. ARCHER, JR.

GLENN L. ARCHER, JR.
Assistant Attorney General
Tax Division
Department of Justice
Washington, D.C. 20530
Counsel for the Appellee

Dated: This 15th day of February, 1984.

CERTIFICATE OF SERVICE

It is hereby certified that service of the foregoing Motion to Dismiss Appeal for Lack of Jurisdiction has been made on opposing counsel on this 15th day of February, 1984, by mailing a copy thereof in an envelope, with postage prepaid, properly addressed to them as follows:

Edward B. Benjamin, Jr., Esquire
Robert W. Nuzum, Esquire
Jones, Walker, Waechter, Poitevent,
Carrere & Denegre
225 Baronne Street, 21st Floor
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MICHAEL L. PAUP

MICHAEL L. PAUP
Attorney

APPENDIX "D"

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 84-4003

JAMES H. RUTTER and MARIE R. RUTTER
and J. H. RUTTER REX MANUFACTURING
COMPANY, INC.,

Petitioners,

versus

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Appeal from the United States Tax Court

Before REAVLEY, RANDALL and WILLIAMS, Circuit Judges.

BY THE COURT:

IT IS ORDERED that respondent's motion to dismiss the appeal is granted.

Filed March 8, 1984

APPENDIX "E"

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 84-4003

JAMES H. RUTTER and MARIE R. RUTTER
and J. H. RUTTER REX MANUFACTURING
COMPANY, INC.,

Petitioners,

versus

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Appeal From the Decision of the United States Tax Court

ON PETITION FOR REHEARING AND
SUGGESTION FOR REHEARING EN BANC

(April 6, 1984)

Before REAVLEY, RANDALL and WILLIAMS, Circuit Judges.

PER CURIAM:

(✓) The Petition for Rehearing is DENIED and no member of this panel nor Judge in regular active service on the Court having requested that the Court be polled on rehearing en banc, (Federal Rules of Appellate Procedure and

Local Rule 35) the Suggestion for Rehearing En Banc is DENIED.

( ) The Petition for Rehearing is DENIED and the Court having been polled at the request of one of the members of the Court and a majority of the Circuit Judges who are in regular active service not having voted in favor of it, (Federal Rules of Appellate Procedure and Local Rule 35) the Suggestion for Rehearing En Banc is also DENIED.

( ) A member of the Court in active service having requested a poll on the reconsideration of this cause en banc, and a majority of the judges in active service not having voted in favor of it, rehearing en banc is DENIED.

ENTERED FOR THE COURT:

/S/ Norman M. Reavley
United States Circuit Judge

No. 83-2124

In the Supreme Court of the United States

OCTOBER TERM, 1984

JAMES H. RUTTER AND
MARIE R. RUTTER AND J. H. RUTTER REX
MANUFACTURING COMPANY, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

REX E. LEE
Solicitor General
Department of Justice
Washington, D. C. 20530
(202) 633-2217

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In the Supreme Court of the United States

OCTOBER TERM, 1984

No. 83-2124

JAMES H. RUTTER AND
MARIE R. RUTTER AND J. H. RUTTER REX
MANUFACTURING COMPANY, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

Petitioners contend that a pretrial order of the Tax Court determining the party upon whom the burden of proof would rest was a final "decision" immediately appealable to the court of appeals under Section 7482(a) of the Internal Revenue Code.

1. Pursuant to Section 534(b) of the Code,[1] the Commissioner notified petitioner J.H. Rutter Rex Manufacturing Company[2] that he planned to issue a notice of deficiency

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[1]Unless otherwise noted, all statutory references are to the Internal Revenue Code of 1954 (26 U.S.C.), as amended (the Code or I.R.C.).

[2]The corporate petitioner's case in the Tax Court was consolidated with that of James H. and Marie R. Rutter, two of the corporation's principals. The term "petitioner" as used herein refers to the corporation.

that would include an amount with respect to the accumulated earnings tax imposed by Code Section 531. Petitioner timely submitted a statement under Section 534(c) setting forth seven grounds on which it proposed to rely to establish that its earnings "ha[d] not been permitted to accumulate beyond the reasonable needs of the business." The Commissioner subsequently issued a notice of deficiency asserting against petitioner an accumulated earnings tax liability of $446,658 for 1977 and $598,077 for 1978 (Doc. 26).[3]

Petitioner sought redetermination of the deficiency in the Tax Court (Doc. 5). In August 1983, petitioner moved to shift to the Commissioner the burden of proof with respect to the seven grounds enumerated in the statement it had earlier filed (Doc. 14).[4] Following a hearing, the Tax Court issued an order denying petitioner's motion with respect to the first five grounds and granting its motion with respect to the other two (Pet. App. A1-A19). Petitioner filed a notice of appeal from that order (Doc. 28).

The Commissioner moved to dismiss the appeal for lack of jurisdiction, contending that the appeal was interlocutory and was not taken from a final "decision" of the Tax Court (Pet. App. A20-A21). The court of appeals granted

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[3]"Doc." references are to the original documents as numbered by the Clerk of the Tax Court.

[4]Section 534(a)(2) generally provides that if the taxpayer in an accumulated earnings tax case has submitted the statement described in Section 534(c), the burden of proof in the Tax Court shall "be on the Secretary with respect to the grounds set forth in such statement in accordance with the provisions of such subsection." The regulations provide that the burden of proof will not shift to the Commissioner if "the ground or grounds on which the taxpayer relies are not relevant to the [Commissioner's] allegation, or if relevant, the statement does not contain facts sufficient to show the basis thereof." Treas. Reg. § 1.534-2(b)(2).

that motion and dismissed the appeal in an unpublished judgment order (*id.* at A26). A petition for rehearing with suggestion of rehearing en banc was denied on April 6, 1984 (*id.* at A27-A28).

2. Section 7482(a) grants the courts of appeals jurisdiction to review "decisions" of the Tax Court. Section 7459(c) provides that "[a] decision of the Tax Court (except a decision dismissing a proceeding for lack of jurisdiction) shall be held to be rendered upon the date that an order specifying the amount of the deficiency is entered in the records of the Tax Court." Reading these two Sections together, the courts of appeals have generally held that the term "decision" as used in Section 7482(a) refers to two (and only two) types of action by the Tax Court: (1) an order dismissing the proceeding before it for lack of jurisdiction; and (2) an order formally determining the amount of a tax deficiency or the absence thereof. See, *e.g.*, *Porter* v. *Commissioner*, 453 F.2d 1231, 1232 (5th Cir. 1972); *Commissioner* v. *Smith Paper, Inc.*, 222 F.2d 126, 129 (1st Cir. 1955); *Kiker* v. *Commissioner*, 218 F.2d 389, 392 (4th Cir. 1955); *Michael* v. *Commissioner*, 56 F.2d 825 (2d Cir. 1932), cert. denied, 296 U.S. 579 (1935). See also *Wilson* v. *Commissioner*, 564 F.2d 1317, 1318 (9th Cir. 1977), cert. denied, 439 U.S. 832 (1978) (order denying a taxpayer's motion to amend his pleadings is an appealable decision where "[t]he order ha[s] the effect of dismissing the * * * ~~the~~ petition * * * for lack of jurisdiction"); *Commissioner* v. *S. Frieder & Sons*, 228 F.2d 478, 482 (3d Cir. 1955) (Tax Court order striking Commissioner's deficiency claim is an appealable decision where the effect is "to decide that it has no such jurisdiction to redetermine the tax"). Cf. *United States* v. *California Eastern Line, Inc.*, 348 U.S. 351 (1955) (Tax Court order dismissing case on the ground that no renegotiable contract existed was an appealable "decision").

Some courts have expanded the definition of "decision" as used in Section 7482(a) to include a third category of Tax Court orders — those that finally "dispose[] of the entire proceeding before" the Tax Court. *Louisville Builders Supply Co.* v. *Commissioner*, 294 F.2d 333, 339 (6th Cir. 1961). Most of these cases involve orders denying petitions to intervene. *E.g., Sampson* v. *Commissioner*, 710 F.2d 262, 263 (6th Cir. 1983) (per curiam); *Estate of Dixon* v. *Commissioner*, 666 F.2d 386, 388 (9th Cir. 1982); *Estate of Smith* v. *Commissioner*, 638 F.2d 665, 668 (3d Cir. 1981). The courts in these cases noted that a denial of intervention finally disposes of the would-be intervenor's petition, and that review of his claim would not be available upon the taxpayer's appeal of the Tax Court's decision on the merits. *Sampson*, 710 F.2d at 263; *Estate of Smith*, 638 F.2d at 667-668. The courts also noted that an order denying intervention is an appealable "final order" when issued by a federal district court. *Estate of Dixon*, 666 F.2d at 388 (citing cases); *Estate of Smith*, 638 F.2d at 668 (same).

The common thread running through these cases is that an appeal can be taken only from a final decision of the Tax Court. See, *e.g., Estate of Dixon*, 666 F.2d at 388; *Estate of Smith*, 638 F.2d at 668; *Handshoe* v. *Commissioner*, 252 F.2d 328, 329 (4th Cir. 1958) (per curiam). Interlocutory orders of the Tax Court, like those issued by federal district courts, are not subject to immediate appeal. *Estate of Dixon*, 666 F.2d at 388; *Estate of Smith*, 638 F.2d at 668. See *Ryan* v. *Commissioner*, 680 F.2d 324, 326-327 (3d Cir. 1982) (Tax Court order denying motion for summary judgment is not an appealable "decision"); *Licavoli* v. *Commissioner*, 318 F.2d 281, 282 (6th Cir. 1963) (per curiam) (Tax Court order striking certain defenses is not an appealable "decision"); *Ceco Steel Products Corp.* v. *Commissioner*, 150 F.2d 698, 699 (8th Cir. 1945) ("intermediate order governing only the course of procedure before

the Tax Court" is not an appealable "decision"); *Michael*, 56 F.2d at 825 (Tax Court order granting severance motion is not an appealable "decision").[5]

The order of the Tax Court at issue here plainly was not a final "decision" immediately appealable to the court of appeals under the principles outlined above. That order did not establish a deficiency in tax or the absence thereof. It did not dismiss the case for lack of jurisdiction. And it did not in any sense finally dispose of the entire proceeding before the Tax Court. All the order did was determine, prior to a trial on the merits, the allocation as between petitioner and the Commissioner of the burden of proof with respect to the seven factual issues raised by petitioner's Section 534(c) statement. The interlocutory nature of that order could scarcely be plainer. See, *e.g.*, *United States* v. *Margiotta*, 662 F.2d 131, 140 n.23 (2d Cir. 1981) (characterizing as interlocutory and hence nonappealable a ruling whose effect was "merely [to] present the Government with a heavier burden of proof"); *Arnold* v. *United States*, 404 F.2d 953, 958 n.6 (Ct. Cl. 1968) (characterizing as interlocutory a trial commissioner's order respecting burden of proof). This Court noted in *Catlin* v. *United States*, 324 U.S. 229, 233 (1945), that "[a] 'final decision' generally is one which ends the litigation on the merits and leaves nothing for the court to do but execute the judgment." The Tax Court's burden-of-proof ruling did not have that effect.

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[5]The purpose of restricting appeals to final decisions is "to combine in one review all stages of the proceeding that effectively may be reviewed and corrected if and when final judgment results." *Cohen* v. *Beneficial Loan Corp.*, 337 U.S. 541, 546 (1949). In this way, courts avoid the fragmentary and piecemeal review that would be caused by a succession of separate appeals from the various rulings to which a litigation may give rise. See *Cobbledick* v. *United States*, 309 U.S. 323, 324-326 (1940).

3. Accordingly, petitioners err in contending (Pet. 7-11) that the circuits are in conflict, in any way material to this case, about the meaning of the term "decision" as used in Section 7482(a). As we have noted, the courts have generally held that a "decision" of the Tax Court means a decision of the type referred to in Section 7459(c) — viz., an order dismissing the proceeding for lack of jurisdiction or determining the amount of a tax deficiency. Some courts have also held, where they have been required to address the question, that a "decision" may include certain other final orders (such as orders denying motions to intervene) that dispose of the entire proceeding and that would not be reviewable absent an immediate appeal. But the courts have uniformly held that an interlocutory order, which does not dispose of the entire case and which can be reviewed in the normal course upon appeal of the Tax Court's decision on the merits, is not a "decision" subject to immediate review. Since the order at issue here — a pretrial order allocating the burden of proof — was clearly interlocutory, petitioner could not prevail under any of the cases it cites.[6]

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[6]The cited cases (Pet. 7-8) are either inapposite or do not stand for the proposition for which petitioner cites them. As we have noted (see page 4, *supra*), the courts in *Ryan* v. *Commissioner, supra*, and *Licavoli* v. *Commissioner, supra*, held that certain interlocutory orders of the Tax Court were not appealable decisions. The courts in *Wilson* v. *Commissioner, supra*, and *Commissioner* v. *S. Freider & Sons, supra*, held that orders striking certain pleadings were appealable decisions, but only because the orders had the effect of dismissing the case for lack of jurisdiction. The court in *Louisville Builders Supply Co.* v. *Commissioner, supra*, held that an order compelling the taking of a deposition was an appealable decision, but that order was "entered by the Tax Court in a so-called Special Proceeding initiated for the sole purpose of obtaining such order" (294 F.2d at 336), in a situation where a notice of deficiency had not yet been issued. The three other cases petitioner cites (Pet. 7) involve appeals of orders denying motions to intervene.

4. Finally, there is no merit to petitioner's contention (Pet. 16-23) that it will be unfairly prejudiced absent an immediate appeal of the Tax Court's burden-of-proof ruling. "*Every* interlocutory order involves, to some degree, a potential loss or harm." *Ryan* v. *Commissioner*, 517 F.2d 13, 19 (7th Cir.), cert. denied, 423 U.S. 892 (1975) (emphasis in original). But that risk "must be balanced against the need for efficient federal judicial administration, the need for the appellate courts to be free from the harassment of fragmentary and piecemeal review of cases otherwise resulting from a succession of appeals from the various rulings which might arise during the course of litigation" (*ibid.*). Accord, *Borden Co.* v. *Sylk*, 410 F.2d 843, 846 (3d Cir. 1969). Even if the Tax Court erred in allocating the burden of proof, petitioner will suffer no harm if it prevails in its claim that it did not unreasonably accumulate earnings (see *W. W. Windle Co.* v. *Commissioner*, 550 F.2d 43 (1st Cir. 1977)), or if the location of the burden of proof turns out to be irrelevant to the Tax Court's ultimate conclusion (*e.g.*, *Raymond I. Smith, Inc.* v. *Commissioner*, 292 F.2d 470, 474 (9th Cir.), cert. denied, 368 U.S. 948 (1961)).[7] At all events, petitioner's interests can be fully protected by an appeal in the normal course following a final decision by the Tax Court, if that decision is adverse to it.

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[7]Petitioner claims (Pet. 18-19) that, absent an immediate appeal of the burden-of-proof ruling, its effort to "formulate [its] trial evidence and strategy" may be prejudiced or compromised. But this risk is present whenever an interlocutory order (such as an order respecting the introduction of testimony or evidence) is involved. A litigant is often faced with a choice between altering his trial strategy to comply with the trial court's rulings, or standing his ground and presenting his claims to the appellate court following an adverse decision on the merits. But the existence of such a choice does not entitle a party to immediate appeal of interlocutory orders.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

REX E. LEE
Solicitor General

OCTOBER 1984

DOJ-1984-10